STATE OF VERMONT
PUBLIC SERVICE BOARD

Docket No. 7662

Petition of Vermont Electric Cooperative, Inc. for Approval to Issue up to $9 Million in Secured First Mortgage Bonds and to Incur Secured/Unsecured Short-Term Obligations Under One or More Revolving Credit Agreements not to Exceed $20 Million	))))))

Order entered: 9/29/2010

I. Introduction

On July 22, 2010, Vermont Electric Cooperative, Inc. ("VEC" or "the Company") filed a petition (the "Petition") pursuant to 30 V.S.A. § 108 with the Vermont Public Service Board ("Board") seeking approval to: (1) issue first-mortgage bonds in an amount not to exceed $9 million and secured under its First Mortgage Indenture (the "Bonds"); and (2) issue secured and/or unsecured short-term indebtedness in connection with one or more proposed revolving credit facilities ("credit lines" or "credit facilities") in a maximum principal amount of $20 million. The proceeds of the Bonds will be used to repay outstanding principal under VEC's existing short-term lines of credit, to fund additional capital improvements, and to finance certain investments in Vermont Transco, LLC ("Transco"). In addition, the credit lines will be used for working capital and the issuance of letters of credit to support purchase power agreements. The Petition was supported by the prefiled testimony of Michael Bursell, the Company's Chief Financial Officer, and by accompanying attachments.

On August 27, 2010, the Vermont Department of Public Service ("DPS") submitted a letter to the Board stating that it believes that the Petition is consistent with the general good of the state, and recommending approval of the Petition without a hearing. The DPS also filed its Determination Under 30 V.S.A. § 202(f) with the Board on August 27, finding that the issuance of long-term and short-term debt as set forth in the Petition is consistent with the *Vermont Electric Plan*.

I have reviewed the Petition, the supporting testimony, and accompanying documents. I conclude that approval of VEC's Petition pursuant to 30 V.S.A. §108(a) is appropriate and that such approval may occur without hearing. Based upon the evidence of record, including the DPS letters of August 27, 2010, I hereby report the following findings and conclusion to the Board in accordance with 30 V.S.A. § 8.

II. Findings

1. Vermont Electric Cooperative, Inc., is a company as defined by 30 V.S.A. § 201. Petition at 1.

2. On June 23, 1997, in Docket No. 5971, the Board issued its decision authorizing VEC to issue Mortgage Bonds under a First Mortgage Indenture between VEC and Bank of New York (the "Indenture"). Petition at 1.

3. The Indenture encumbers substantially all of the assets of VEC, including substantially all of VEC's operating real estate, plant and equipment, with limited exceptions. Petition at 1.

4. VEC requests Board approval to issue the Bonds under its existing Indenture. The principal amount of the Bonds will not exceed $9 million. The proceeds of the Bonds will be used to: (1) repay the principal amount outstanding under VEC's existing short-term line of credit; (2) finance certain capital improvements as identified in VEC's capital budget plan; (3) pay a portion of the costs of issuance of the Bonds; and (4) provide liquidity necessary for VEC to participate in Transco's anticipated 2010 membership unit issuance. VEC anticipates that the Bonds will be issued in December 2010. Bursell pf. at 3; schedule A.

5. VEC expects to spend approximately $9,650,000 as part of its 2010 capital budget plan to finance capital improvements identified in a report by MPR Associates,[1] in the Business Process Review and Audit performed by Stone & Webster Management Consultants, Inc., and in the Company's Integrated Resource Plan submitted to the Board on June 30, 2008. VEC contemplates the issuance of $9 million of first-mortgage bonds to partially fund the capital improvements contained in its capital plan, to pay down its line of credit, and to acquire Transco

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1. VEC previously submitted a work plan in relation to the investigation conducted by MPR Associates of an incident which occurred at VEC's Richford substation. *See* Investigation into Vermont Electric Cooperative, Inc.'s Service Quality and Reliability, Docket No. 7273, Order of April 4, 2008, at 2, 9.

units. Bursell pf. at 4.

6. VEC has approached and will select between its two most significant lenders, CoBank ACB ("CoBank") and the National Rural Utilities Cooperative Finance Corporation ("CFC"), to determine which institution would be willing to provide VEC with the requested financing. Both CoBank and CFC are holders of VEC's bonds previously issued under the Indenture. Both CoBank and CFC provide for a return of patronage capital as the loans are repaid, reducing the effective borrowing rates. The return of patronage capital has ranged from 40 basis points to 75 basis points annually. Bursell pf. at 4-5.

7. CFC has provided VEC with two financing options that include financing using CFC's traditional loan program or the CFC Advantage program. The CFC Advantage program is a partnership with the Federal Agricultural Mortgage Corporation ("Farmer Mac"), and CFC that provides for CFC to administer the Bonds pursuant to VEC's Indenture, but is not eligible for the return of CFC patronage capital. Under CFC's traditional loan program, VEC would be required to borrow additional funds in order to purchase loan capital term certificates ("LCTC's") as a condition of membership in CFC; however, as a member of CFC, VEC will become entitled to accrue patronage capital in CFC. In the event that CFC is selected as the lender for the Bonds under the traditional loan program, VEC expects to incur additional indebtedness of $225,000 to purchase the LCTC's. Bursell pf. at 5.

8. VEC is considering maturities for the Bonds of between fifteen to thirty years depending upon the impact the amortization schedules will have on cash flow based upon the interest rates then available for the term. VEC will have the option to choose either a fixed or variable rate, or a combination of both, and may elect to fix the interest rate on all or a portion of the Bonds for a period from one to thirty years. Current market rates show CoBank variable rates at 3.51% and CFC variable rates at 4.95%. Five-year and thirty-year fixed rates quoted by CoBank are approximately 3.53% and 5.78%, respectively, and CFC's five-year and thirty-year rates are 5.03% and 7.43%, respectively. VEC will monitor the interest rates available from these lenders to select the most advantageous rate. Principal and interest payments will be due quarterly based on a level debt-service schedule. If CFC Advantage is chosen, payments will be made on a semi-annual basis. Bursell pf. at 7-8.

9. The Bonds will largely finance long-term improvements as part of VEC's capital plan. VEC has also funded system improvements through borrowings under its line of credit. The proceeds of the Bonds will be used in part to convert those short-term borrowings into long-term debt thereby amortizing the costs of those improvements over the useful life of the assets. In addition, such a reduction in short-term debt will free up additional capacity on VEC's credit line for banks to issue letters of credit, as needed, under VEC's power purchase agreements. Bursell pf. at 8-9.

10. Up until the time of issuance of the Bonds, VEC will assess whether an anticipated issuance of equity units by Transco will take place and if VEC will be permitted to purchase a portion of those units.[2] VEC's ratings agencies are supportive of some investments in Transco given the return offered by Transco equity. In addition, interest rates are at historical lows, and as a result, with an expected fixed return of 12.51%, the spread between current interest rates and the anticipated Transco equity returns is expected to result in positive impacts on VEC's times-interest-earned ratio ("TIER") beginning in the first year. VEC modeled the impact of an assumed $3.5 million investment in Transco which reflects positive growth in TIER as a result of excess dividend income (after debt service) over a twenty-year period. In the event that it appears that VEC will not participate in the issuance of Transco equity as of the date of the issuance of the Bonds, VEC would reduce the principal amount of the Bonds by the amount of its anticipated investment of approximately $3.5 million. Bursell pf. at 9-10; schedule B.

11. VEC currently has revolving credit agreements with CoBank and CFC in the aggregate principal amount of $20 million that is available for either short-term loans or support for letters of credit. If a letter of credit is issued, the principal amount available under the corresponding credit line is reduced by that amount. The credit facilities are split between CoBank and CFC, with a $10 million line of credit residing with CoBank, which is available for short-term working capital loans, and a $10 million letter of credit facility with CFC primarily used to support VEC's power purchase agreements. The letter of credit facility with CFC is scheduled to mature on March 31, 2011. CFC has notified VEC of CFC's intent to increase its commitment fee, at

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2. VEC has participated indirectly in issuances by Transco in 2008 and 2009 under the terms of an agreement with the Vermont Public Power Supply Authority. *See* Docket Nos. 7487 and 7569.

maturity, to 25 basis points of the available amount of the facility. VEC seeks to mitigate this fee increase by entering into new credit agreements with CFC and Cobank whereby the existing aggregate availability of $20 million will be reallocated among the lenders providing Cobank with a share of the letter of credit facility. Accordingly, VEC proposes to retain approximately $3 million in letter of credit availability with CFC, and to utilize CoBank for a letter of credit facility with capacity of approximately $7 million. Bursell pf. at 12-13.

III. Discussion & Conclusion

In its Petition, VEC contends that its choice of amortization schedules for the Bonds of fifteen to thirty-years will be based upon the interest rates then available and the potential impacts on its cash flow.[3] VEC's lenders have provided the Company with a choice between variable and fixed rates as set out in Finding No. 8, above. Corporate lending rates, although currently at historic lows, remain vulnerable to potential volatility in the credit markets. Due to this uncertainty, I recommend that the Board adopt a condition requiring VEC to provide advance notice to the Board prior to closing of an increase greater than 100 basis points in the interest rate it selects from those offered by its lenders as set out in the findings, above.

Based on the evidence, I conclude that VEC's petition to issue the Bonds in an amount not to exceed $9 million with either CFC or CoBank, and secured under its First Mortgage Indenture, will be consistent with the general good of the state. The Bonds will provide a source of funding for VEC to improve its balance sheet by converting short-term debt to long-term debt, make system improvements pursuant to its 2009 capital budget plan, and to participate in the anticipated 2010 issuance of membership units by Transco. In addition, VEC's proposed modifications to its maturing short-term credit lines will allow VEC to reduce its exposure to expected fee increases and offer greater diversification of its letter of credit availability between its lenders. Therefore, I find that approval of VEC's request for long-term indebtedness and the proposed reallocation of its credit lines, as described above, is consistent with the general good of the state and recommend that the Board issue an order to that effect.

The parties have waived the opportunity for review of the Proposal for Decision, briefing,

3. Bursell pf. at 8-7.

and oral argument, in accordance with 3 V.S.A. § 811.

Dated at Montpelier, Vermont this 28th day of September, 2010.

s/ Jay E. Dudley
Jay E. Dudley
Hearing Officer

IV. Order

It Is Hereby Ordered, Adjudged and Decreed by the Public Service Board ("Board") of the State of Vermont that:

1. The Findings, Conclusion, and recommendations of the Hearing Officer are adopted.

2. The Board consents to the issuance by Vermont Electric Cooperative, Inc. ("VEC") of first mortgage bonds in an amount not to exceed $9 million and secured under its First Mortgage Indenture, with either National Rural Utilities Cooperative Finance Corporation or CoBank, ACB, as lender, and to utilize the interest-rate options as set forth in the findings, above. In addition, the Board consents to VEC's proposed modification and reallocation of its revolving line of credit facilities with those lenders in the aggregate amount of $20 million.

3. This Order does not constitute approval of any particular capital or operating expenditure nor the underlying capital structure that VEC may implement. Nothing in this approval shall preclude the Vermont Department of Public Service ("DPS") or any other party, or the Board, from reviewing and/or challenging those expenditures and/or VEC's resulting capital structure in any future proceeding.

4. VEC shall inform the Board and the DPS of any material change in the terms and conditions of the financing, if any, prior to closing.

5. VEC shall inform the Board prior to closing of an increase greater than 100 basis points in the interest rate it selects from those offered by its lenders as set out in the findings, above.

6. VEC shall provide the Board and the DPS with a complete set of final executed documents when they are available.

Dated at Montpelier, Vermont, this 29th day of September, 2010.

s/ James Volz	)	
	)	PUBLIC SERVICE
	)	
s/ David C. Coen	)	BOARD
	)	
	)	OF VERMONT
s/ John D. Burke	)	

OFFICE OF THE CLERK

FILED: September 29, 2010

ATTEST: s/ Susan M. Hudson
Clerk of the Board

NOTICE TO READERS: This decision is subject to revision of technical errors. Readers are requested to notify the Clerk of the Board (by e-mail, telephone, or in writing) of any apparent errors, in order that any necessary corrections may be made. (E-mail address: psb.clerk@state.vt.us)

Appeal of this decision to the Supreme Court of Vermont must be filed with the Clerk of the Board within thirty days. Appeal will not stay the effect of this Order, absent further Order by this Board or appropriate action by the Supreme Court of Vermont. Motions for reconsideration or stay, if any, must be filed with the Clerk of the Board within ten days of the date of this decision and order.